



## BOARD OF EQUALIZATION

**BUSINESS TAXES COMMITTEE MEETING MINUTES**

HONORABLE BETTY T. YEE, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

MEETING DATE: SEPTEMBER 16, 2008, TIME: 9:30 A.M.

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**ACTION ITEMS & STATUS REPORT ITEMS****Agenda Item No: 1****Title: Proposed regulatory changes to clarify application of tax to alteration charges****Issue/Topic:**

Should Regulation 1506, *Miscellaneous Service Enterprises*, and Regulation 1524, *Manufacturers of Personal Property*, be amended to clarify the application of tax to alteration charges by clothes cleaners and dyers?

**Committee Discussion:**

Interested parties explained that some dry cleaners make infrequent sales of items such as lint brushes and collar stays as a convenience to their customers. Dry cleaners pay tax on these items when they purchase them and the cleaner's mark-up is minimal. Interested parties believe that the cost of maintaining records and filing sales tax returns just for these sales is burdensome, and asked the Board Members to consider exempting dry cleaners from retailer status when the cleaner's sales of tangible personal property are a minimal amount such as under \$400 or \$600 annually.

Board Members discussed the need to move ahead with the proposed regulation revisions in order to clarify the current application of tax to alteration charges. Board Members also discussed the need for staff to provide education and outreach to dry cleaners, including making those materials available in other languages. Staff agreed to continue to work with the dry cleaner associations to develop and distribute written publications and training.

Board Members also asked staff to work with the dry cleaner's associations to better understand dry cleaners' record keeping systems. In addition, Board Members asked staff to pursue a separate process to consider a de minimis standard for obtaining a seller's permit under the occasional sale rules.

**Committee Action/Recommendation/Direction:**

Upon motion by Dr. Chu, seconded by Ms. Mandel, the Committee unanimously approved and authorized for publication the proposed regulatory amendments. There is no operative date, and implementation will take place 30 days after approval by the Office of Administrative Law. Copies of the proposed amendments to Regulations 1506 and 1524 are attached.

**Agenda Item No: 2****Title: Proposed regulatory changes regarding a franchisee's relief from liability to pay tax based on erroneous advice provided to franchisor****Issue/Topic:**

Should Regulation 1705, *Relief from Liability*, be revised to explain when a franchisee is relieved from the liability to pay tax based on erroneous written advice provided to its franchisor?

**Committee Discussion:**

Staff described the proposed revisions and explained that the revisions clarify the current application of tax.

**Committee Action/Recommendation/Direction:**

Upon motion by Dr. Chu, seconded by Ms. Mandel, the Committee unanimously approved and authorized for publication the proposed regulatory amendments. There is no operative date, and implementation will take place 30 days after approval by the Office of Administrative Law. A copy of the proposed amendments to Regulation 1705 is attached.

/s/ Betty T. Yee

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Honorable Betty T. Yee, Committee Chair

/s/ Ramon J. Hirsig

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Ramon J. Hirsig, Executive Director

BOARD APPROVED

at the September 17, 2008 Board Meeting

/s/ Diane Olson

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Diane Olson, Chief  
Board Proceedings Division

## **Proposed Amendments to Regulation 1506**

### **Regulation 1506. Miscellaneous Service Enterprises.**

#### **(a) LICENSED ARCHITECTS.**

(1) IN GENERAL. Fees paid to licensed architects for their ability to design, conceive or communicate ideas, concepts, designs, and specifications are not subject to tax. Any plans, specifications, renderings or models or other instruments of service provided by a licensed architect under a licensed architect's contract or commission are integral to the licensed architect's services and are not subject to tax. The licensed architect is the consumer of any tangible personal property, including plans, specifications, renderings or models, used or transferred in the performance of professional services notwithstanding the fact that a fee may be added to the cost of the property and separately stated on a billing to the customer. If after the completion of the contract or commission the licensed architect provides additional copies of the original plans or specifications, or any models or renderings of an existing structure, the architect is regarded as making a sale of such copies, models or renderings.

(2) LICENSED ARCHITECT. A "licensed architect" is defined under the Business and Professions Code Chapter 3, Division 3, Section 5500 as follows:

"As used in this chapter, architect means a person who is licensed to practice architecture in this state under the authority of this chapter."

A licensed architect preparing or being in responsible control of plans, specifications, and instruments of service is required to affix to those plans, specifications, and instruments of service their stamp or seal which bears the licensee's name, his or her license number, the legend "Licensed Architect" and the legend "State of California," and which shall provide a means of indicating the renewal date of the license.

(3) ARCHITECTURAL PERSPECTIVISTS AND MODELERS. Architectural perspectivists do not act as "licensed architects." Architectural perspectivists are the retailers of renderings, prints and drawings they provide to architects or other consumers and tax applies to their entire charge for such items. Modelers do not act as "licensed architects." Modelers are the retailers of models they provide to architects or other consumers, and tax applies to their entire charge for such items.

(4) Licensed architects who produce renderings, prints, drawings or models pursuant to a contract that includes professional architectural services are not retailers of the renderings, prints, drawings or models they provide pursuant to that contract for architectural services. Tax does not apply to their charge for such items.

**(b) BARBERS, BEAUTY SHOP OPERATORS, AND SHOE POLISHERS, ~~Launderers and Cleaners.~~** ~~—(1) In General.~~ Barbers, beauty shop operators, and shoe polishers, ~~launderers and cleaners~~ are the consumers of the supplies and other property used in performing their services, and tax applies with respect to the sale to them of the supplies and other property. They are retailers, however, of ~~any such supplies, or of used articles,~~ or other tangible personal property, which they sell to ~~consumers~~ customers in the regular course of business, and tax applies to the gross receipts from such sales.

## **Proposed Amendments to Regulation 1506**

~~(2) Rentals. Launderers and cleaners are the consumers of linen supplies and similar articles, including towels, uniforms, coveralls, shop coats, dust cloths, and similar items, rented to others when an essential part of the rental contract is the furnishing of the recurring service of laundering or cleaning of the articles rented, and tax applies with respect to the sale to them of such articles.~~

### **(c) CLOTHES CLEANERS AND DYERS**

(1) CLOTHES CLEANING – IN GENERAL. Persons who provide clothes-cleaning services are consumers of the supplies and other materials used in performing their cleaning services, and tax applies to the sale to them of the supplies and other materials and not to their charges for such services.

(2) RENTALS. Clothes cleaners are the consumers of linen supplies and similar articles, including towels, uniforms, coveralls, shop coats, dust cloths, and similar items, rented to others when an essential part of the rental contract is the furnishing of the recurring service of laundering or cleaning of the articles rented, and tax applies with respect to the sale to them of such articles.

(3) CLOTHES DYEING – IN GENERAL. Persons who provide dyeing services are retailers, not consumers, when their charges are for the dyeing of new fabrics, garments, or other such items and tax applies to their gross receipts from such sales. Persons who dye new items are required to hold a seller's permit.

Dyers are consumers of the supplies and other materials used in dyeing used fabrics, garments, or other such items and tax applies to the sale to them of the supplies and other materials and not to their charges for their dyeing services.

(4) ALTERATION OF GARMENTS – IN GENERAL. For the purposes of this subdivision (c), alteration of garments means and includes any work performed upon new or used men's, women's and children's clothing to meet the requirements of the customer whether the work involves the addition of material to the garment, removal of material, refitting, or repairing. Alteration of garments does not mean or include the process of dyeing garments. Alteration of garments also does not mean or include work performed upon new or used personal and household items such as handbags, stuffed animals, bedding, and draperies. The application of tax to a clothes cleaner's or a dyer's charges for the alteration of personal or household items is explained in Regulation 1524.

(A) Alteration of Garments by Clothes Cleaning or Dyeing Establishments. A clothes cleaning or dyeing establishment, including wet cleaners (e.g., launderers) and dry cleaners, means and includes a clothes cleaner or dyer who (1) operates a location or locations as a pickup and delivery point for garment cleaning, or (2) provides spotting and pressing services on the premises, but not garment cleaning, or (3) operates a garment cleaning or dyeing plant on the premises.

A clothes cleaner or dyeing establishment described above is the consumer of property used or furnished in the alteration of new or used garments provided that:

1. Seventy-five percent (75%) or more of the establishment's total gross receipts represent charges for garment cleaning or dyeing services, and

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2. No more than twenty percent (20%) of the establishment's total gross receipts during the preceding calendar year were from the alteration of garments.

If a clothes cleaner or dyer is not an establishment as described or does not meet the requirements of this paragraph (A), tax applies to the clothes cleaner's or the dyer's charges for the alteration of garments as explained in Regulation 1524.

**(B) Alteration of Garments by a Third Party.** When a clothes cleaner or dyer who meets the requirements of subdivision (c)(4)(A) contracts with a third party such as a tailor for the alteration of garments instead of performing such alterations itself, the clothes cleaner or dyer is a consumer, not a retailer, of the alterations provided by the third party and may not issue a resale certificate to the third party for such alterations. Tax applies to the third party's charges to the clothes cleaner or dyer for such alterations as explained in Regulation 1524.

(5) MISCELLANEOUS SALE OF ITEMS. Clothes cleaners and dyers, whether or not they meet the requirements of subdivision (c)(4)(A), are retailers of any supplies, used items, or other tangible personal property such as lint brushes, abandoned garments, wood hangers, or novelty items, which they sell to customers in the regular course of business, and tax applies to the gross receipts from such sales. As retailers of tangible personal property, such persons are required to hold a seller's permit.

**(ed) CIRCULATING LIBRARIES.** When circulating libraries, which are engaged in the business of renting books to others, pay tax measured by the purchase price of such books either to the person from whom the books are purchased or to the board, tax does not apply to the amount charged for the rental of such books. Such libraries are retailers of new or used books, which they sell to consumers in the regular course of business, and tax applies to the gross receipts from such sales.

**(de) DENTISTS AND DENTAL LABORATORIES.** Dentists are consumers of the materials, supplies, dental laboratory products and other tangible personal property which they use in performing their services. Tax, accordingly, applies to the sale of the tangible personal property to them.

Dental laboratories are the retailers of the plates, inlays and other products which they manufacture for dentists or other consumers. Tax applies to their entire charges for such products regardless of whether a separate charge or billing is made for materials and manufacturing services.

**(ef) GUN CLUBS.** Gun clubs are consumers, not retailers, of clay pigeons or blue rocks furnished to members or patrons in connection with trapshooting or similar sports even though the charge for the service is measured by the number of clay pigeons or blue rocks used. The tax applies with respect to the sale of such property to the clubs.

**(fg) LICENSED HEARING AID DISPENSERS.** Persons licensed as hearing aid dispensers by the Department of Consumer Affairs, Hearing Aid Dispensers Examining Committee, are consumers of hearing aids furnished or sold by them. The term "hearing aid" includes any necessary accessory or component part of the hearing aid which is fully worn on the body of the user such as cords, connector tubing, ear molds, or batteries, whether the part is sold or furnished

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separately or in conjunction with the hearing aid. The term also includes replacement and repair parts. Tax applies with respect to the sale of such products to licensed hearing aid dispensers.

Tax applies to the retail sale of such products by persons who are not licensed hearing aid dispensers.

**(gh) SUMMER CAMPS.** The tax applies to gross receipts from the sale of meals or other tangible personal property at summer camps, whether operated by municipal or private corporations, or other parties. When a camp qualifies as a school or educational institution, tax, with respect to meals, applies in the same manner as to schools and educational institutions. To qualify as a school or educational institution for purposes of this regulation, the camp must conduct regularly scheduled classes, with required attendance, in charge of qualified instructors.

If a single charge is made for all of the privileges extended by the camp, a segregation must be made and the tax returned on that portion of the total charge representing taxable receipts from the sale of meals or other tangible personal property. In the absence of such a segregation, the taxable receipts from the sale of meals or other tangible personal property shall be determined by the board based on information available to it.

**(hi) TAXIDERMISTS.** Taxidermists are consumers of the materials used in repairing, stuffing and mounting skins, heads, etc., of animals, birds, fish, and the like furnished by their customers, and tax applies with respect to the sale of such property to them. If, however, a separate charge for such property is made on the invoices to the customers at the fair retail selling price, the taxidermist is the retailer of the property and tax applies to such separate charge.

Tax applies to retail sales by taxidermists of skins, heads, mountings or other tangible personal property.

### **(ij) LICENSED VETERINARIANS.**

(1) DEFINITIONS. As used herein:

(A) The term “licensed veterinarian” means any person licensed as a veterinarian by the California Department of Consumer Affairs, Board of Examiners in Veterinary Medicine.

(B) The term “drugs and medicines” includes substances or preparations intended for use in the diagnosis, cure, mitigation, treatment, or prevention of disease in animals and which is commonly recognized as a substance or preparation intended for this use. The term includes legend drugs, pills and capsules (other than vitamins), liquid medications, injected drugs, ointments, vaccines, intravenous fluids, and medicated soaps if those soaps are available only to veterinarians. The term does not include vitamins, shampoos, pet foods, prescription diet foods, artificial diets, flea powders, and flea sprays.

(C) The term “professional services” includes the diagnosis and treatment of disease or trauma in animal life. It also includes the administration of drugs and medicines by means of, for example, injection, intravenous solution, or oral or bodily application.

## **Proposed Amendments to Regulation 1506**

### **(2) APPLICATION OF TAX.**

**(A)** Licensed veterinarians are consumers of drugs and medicines which they use or furnish in the performance of their professional services. Accordingly, tax does not apply to a licensed veterinarian's charges to clients for such drugs and medicines, whether or not separately stated. Licensed veterinarians are also consumers of tangible personal property, other than drugs and medicines, which they use or which they furnish to clients without a separately stated charge. Tax applies to the sales of such drugs, medicines and other items to licensed veterinarians except:

1. Operative April 1, 1996, drugs or medicines which are purchased to be administered to animal life as an additive to feed or drinking water of food animals (as defined in Regulation 1587 (18 CCR 1587), "Animal Life, Feed, Drugs and Medicines") or of non-food animals which are being held for sale in the regular course of business, and the primary purpose of the drugs or medicines is the prevention and control of disease, or

2. Operative January 1, 1997, drugs or medicines which are purchased to be administered directly (e.g., orally, by injection, or by application to the body) to food animals and the primary purpose of the drugs or medicines is the prevention or control of disease of the food animals. Veterinarians remain consumers of drugs and medicines administered directly to non-food animals.

**(B)** Licensed veterinarians are retailers of drugs and medicines which they furnish for a consideration without performing specific related professional services. Licensed veterinarians are also retailers of tangible personal property, other than drugs and medicines, which they furnish to clients for a separately stated charge. Unless otherwise exempt, tax applies to charges made by licensed veterinarians to clients for such drugs, medicines and other items. See Regulation 1587(18 CCR 1587), "Animal Life, Feed, Drugs and Medicines" for exemption for sales of feed, drugs, or medicines for certain animals. Tax applies to separately stated charges made for X-rays if the X-rays are delivered to clients.

## Proposed Amendments to Regulation 1524

### Regulation 1524. Manufacturers of Personal Property.

(a) **IN GENERAL.** Tax applies to the gross receipts from retail sales (i.e., sales to consumers) by manufacturers, producers, processors, and fabricators of tangible personal property the sale of which is not otherwise exempted. The measure of the tax is the gross receipts of, or sales price charged by, the manufacturer, producer, processor, or fabricator, from which no deduction may be taken ~~by the manufacturer~~ on account of the cost of the raw materials or other components purchased, or labor or service costs to create or produce the tangible personal property, or of any step in the manufacturing, producing, processing, or fabricating, including work performed to fit the customer's specific requirements, whether or not performed at the customer's specific request, or any other services that are a part of the sale. In addition, no deduction may be taken on account of interest paid, losses, or any other expense.

#### (b) PARTICULAR APPLICATIONS.

(1) ~~Alterations to New Clothing for Men, Women and Children.~~ ALTERATION OF NEW AND USED ITEMS.

~~(A) Definition of Alteration. "Alteration," as herein used, means and includes any work performed upon new clothing to meet the requirements of a customer, whether the work involves the addition of material to the garment, the removal of material from the garment, the rearranging or restyling of the garment, or any other change therein.~~

(A) Alteration of New Items means and includes any work performed upon new items such as garments, bedding, draperies, or other personal and household items to meet the requirements of the customer, whether the work involves the addition of material to the item, the removal of material from the item, the rearranging or restyling of the item, or otherwise altering the item, when such alterations result in the creation or production of a new item or constitute a step in the creation or production of a new item for the customer.

Charges for the alteration of new items are subject to tax, except as provided in subdivision (c)(4) of Regulation 1506, regardless of whether the charges for the alterations are separately stated or included in the price of the item, or whether the alterations are performed by the seller of the item or by another person. Persons engaged in the producing, processing or fabricating of new items are retailers, not consumers, of the alterations provided to the customer and are required to hold a seller's permit.

(B) Alteration of Used Items means and includes the mending, shortening or lengthening, taking in or letting out, or otherwise altering used items such as garments, bedding, draperies, or other personal and household items when such alterations merely refit or repair the item for the use for which it was created or produced.

Charges for the alteration of used items are not subject to tax. Generally, persons performing the alteration of used items are consumers, not retailers, of the supplies and materials furnished in connection with the alterations, and tax applies to the sale of the supplies and materials to such persons.



## Proposed Amendments to Regulation 1524

Except as provided in subdivision (c)(4) of Regulation 1506, persons performing the alteration of used items are retailers, not consumers, of the supplies and materials furnished in connection with the alterations when the retail value of the supplies and materials is more than 10 percent of the total charge for the alterations, or if the invoice to the customer includes a separate charge for such property. When such persons are retailers, not consumers, tax applies to the fair retail selling price of the supplies and materials to the customer.

When the retail value of the supplies and materials is more than 10 percent of the total charge to the customer, the person performing the alterations must segregate on the invoice to the customer and in its records, the fair retail selling price of the supplies and materials from the charge for the alterations. "Total charge" means the combined total of the retail value of the supplies and materials furnished or consumed as part of the alterations and the labor charges for the alterations.

~~—(B) Application of Tax.~~

~~—1. In General. Charges for alterations to new clothing are subject to tax. It is immaterial whether the charges for the alterations are separately stated or are included in the price of the garment. It also is immaterial whether the alterations are performed by the seller of the garment or by another person.~~

~~—(2) Alterations by Clothes Cleaning or Clothes Dyeing Establishment. A person who operates a clothes cleaning or clothes dyeing establishment is the consumer of property used or furnished in altering new and used clothing, provided that~~

~~—(A) 75 percent or more of the establishment's total gross receipts represent charges for garment cleaning or dyeing services and~~

~~—(B) No more than 20 percent of the establishment's total gross receipts during the preceding calendar year were from the alteration of new and used garments.~~

~~If both requirements are met, sales tax shall not apply to the operator's charges for alterations of new or used clothing. However, that person is a retailer of any other tangible personal property sold to consumers in the regular course of business, and sales tax shall apply to the gross receipts from those sales.~~

(32) PAINTING, POLISHING, FINISHING. Tax applies to charges for painting, polishing, and otherwise finishing tangible personal property in connection with the production of a finished product for consumers, whether the article to be finished is supplied by the customer or by the finisher. Tax does not apply to charges for painting or finishing real property.

## **Proposed amendments to Regulation 1705**

### **Regulation 1705. RELIEF FROM LIABILITY.**

**(a) IN GENERAL.** A person may be relieved from the liability for the payment of sales and use taxes, including any penalties and interest added to those taxes, when that liability resulted from the failure to make a timely return or a payment and such failure was found by the Board to be due to reasonable reliance on:

(1) Written advice given by the Board under the conditions set forth in subdivision (b) below; or

(2) Written advice in the form of an annotation or legal ruling of counsel under the conditions set forth in subdivision (d) below; or

(3) Written advice given by the Board in a prior audit of that person under the conditions set forth in subdivision (c) below. As used in this regulation, the term “prior audit” means any audit conducted prior to the current examination where the issue in question was examined.

Written advice from the Board may only be relied upon by the person to whom it was originally issued or a legal or statutory successor to that person. Written advice from the Board which was received during a prior audit of the person under the conditions set forth in subdivision (c) below, may be relied upon by the person audited or by a legal or statutory successor to that person.

The term “written advice” includes advice that was incorrect at the time it was issued as well as advice that was correct at the time it was issued, but, subsequent to issuance, was invalidated by a change in statutory or constitutional law, by a change in Board regulations, or by a final decision of a court of competent jurisdiction. Prior written advice may not be relied upon subsequent to: (1) the effective date of a change in statutory or constitutional law and Board regulations or the date of a final decision of a court of competent jurisdiction regardless that the Board did not provide notice of such action; or (2) the person receiving a subsequent writing notifying the person that the advice was not valid at the time it was issued or was subsequently rendered invalid. As generally used in this regulation, the term “written advice” includes both written advice provided in a written communication under subdivision (b) below and written advice provided in a prior audit of the person under subdivision (c) below.

#### **(b) ADVICE PROVIDED IN A WRITTEN COMMUNICATION.**

(1) Advice from the Board provided to the person in a written communication must have been in response to a specific written inquiry from the person seeking relief from liability, or from his or her representative. To be considered a specific written inquiry for purposes of this regulation, representatives must identify the specific person for whom the advice is requested. Such inquiry must have set forth and fully described the facts and circumstances of the activity or transactions for which the advice was requested.

(2) A person may write to the Board and propose a use tax reporting methodology for qualified purchases subject to use tax. If the Board concludes that the reporting method reflects the person’s use tax liability for the defined population, then the Board may write to the person approving the use of the reporting method. The approval shall be subject to certain conditions. The following conditions shall be included in the approval:

**(A)** The defined population of the purchases that will be included in the reporting method;

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- (B) The percentage of purchases of the defined population that is subject to tax;
- (C) The length of time the writing shall remain in effect;
- (D) The definition of a significant or material change that will require rescinding the approved reporting method; and
- (E) Other conditions as required.

The written approval of the use tax reporting methodology is void and shall not be relied upon for the purposes of Revenue and Taxation Code section 6596 if the taxpayer files a claim for refund for tax that had been reported based upon this reporting method.

**(c) WRITTEN ADVICE PROVIDED IN A PRIOR AUDIT.** Presentation of the person's books and records for examination by an auditor shall be deemed to be a written request for the audit report. If a prior audit report of the person requesting relief contains written evidence which demonstrates that the issue in question was examined, either in a sample or census (actual) review, such evidence will be considered "written advice from the Board" for purposes of this regulation. A census (actual) review, as opposed to a sample review, involves examination of 100% of the person's transactions pertaining to the issue in question. For written advice contained in a prior audit of the person to apply to the person's activity or transaction in question, the facts and conditions relating to the activity or transaction must not have changed from those which occurred during the period of operation in the prior audit. Audit comments, schedules, and other writings prepared by the Board that become part of the audit work papers which reflect that the activity or transaction in question was properly reported and no amount was due are sufficient for a finding for relief from liability, unless it can be shown that the person seeking relief knew such advice was erroneous.

**(d) ANNOTATIONS AND LEGAL RULINGS OF COUNSEL.** Advice from the Board provided to the person in the form of an annotation or legal ruling of counsel shall constitute written advice only if:

(1) The underlying legal ruling of counsel involving the fact pattern at issue is addressed to the person or to his or her representative under the conditions set forth in subdivision (b) above; or

(2) The annotation or legal ruling of counsel is provided to the person or his or her representative by the Board within the body of a written communication and involves the same fact pattern as that presented in the subject annotation or legal ruling of counsel.

**(e) TRADE OR INDUSTRY ASSOCIATIONS OR FRANCHISORS.** A trade or industry association requesting advice on behalf of its member(s) must identify and include the specific member name(s) for whom the advice is requested for relief from liability under this regulation. A franchisor requesting advice on behalf of its franchisee(s) must identify and include the specific franchisee name(s) for whom the advice is requested for relief from liability under this regulation.

For an identified trade or industry member or franchisee to receive relief based on advice provided in the written communication to the trade or industry association or franchisor, the activity or transactions in question must involve the same facts and circumstances as those presented in the written inquiry by the association or franchisor.